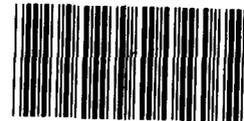


October 1992

# POSTAGE STAMP PRODUCTION

## Private Sector Can Be a Lower Cost Optional Source



148025

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**United States  
General Accounting Office  
Washington, D.C. 20548**

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**General Government Division**

B-236453

October 30, 1992

The Honorable William L. Clay  
Chairman, Committee on Post Office  
and Civil Service  
House of Representatives

The Honorable Frank McCloskey  
Chairman, Subcommittee on  
Postal Operations and Services  
Committee on Post Office and  
Civil Service  
House of Representatives

This report, prepared at your request, reviews the United States Postal Service's initiative to procure postage stamps from the private sector. The report provides information on the private sector stamp production capacity, the price comparability of Bureau of Engraving and Printing and private sector stamps, and the relationship between the Bureau and the Postal Service.

As requested by the Subcommittee, no further distribution of the report will be made until 30 days from the date of the report, unless you publicly release its contents earlier. At that time, copies will be sent to the Senate Committee on Governmental Affairs, the Secretary of the Treasury, and the Postmaster General. Copies will also be provided to other interested parties upon request.

Major contributors to this report are listed in appendix VI. If you have any questions concerning the report, please contact me at (202) 275-8676.

L. Nye Stevens  
Director, Government Business  
Operations Issues

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# Executive Summary

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## Purpose

Producing postage stamps is big business. In fiscal year 1991 the U.S. Postal Service spent \$124 million for approximately 54 billion stamps. Approximately 40 billion stamps were procured from a federal agency, the Bureau of Engraving and Printing, and approximately 14 billion were procured from the private sector. Following a June 1991 hearing that raised questions about the Postal Service's initiative to procure stamps from private sector suppliers, the Chairman of the Subcommittee on Postal Operations and Services, House Committee on Post Office and Civil Service, asked GAO to determine whether (1) the stamp production capacity in the private sector is sufficient for viable competition, (2) the Postal Service monitors stamp quality, (3) the Bureau's prices can be compared with private sector prices, and (4) additional improvements are needed in the relationship between the Bureau and the Postal Service.

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## Background

The Bureau of Engraving and Printing, which is overseen by the Treasurer of the United States, produced all of the nation's stamps from 1894 to 1978. The Postal Service, however, is not legally required to obtain its stamps from a government supplier and since 1978 has contracted out selected stamp issues to determine if stamp costs could be lowered through competitive bidding and if additional sources of stamp production could be developed.

Most stamps are used to post mail. However, some are sold to stamp collectors and never enter the mail stream. These include "philatelic" stamps, which are selected from regular stamp issues for sale through mail order and philatelic windows in some large post offices. Collectors also purchase some stamps through regular retail outlets, such as post offices, vending machines, and retail stores. Stamps retained by collectors are high-profit items because the Postal Service is spared from providing mail delivery service for them. The Postal Service reported revenues of \$162 million from stamps sold to and retained by collectors in fiscal year 1991.

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## Results in Brief

The private sector has sufficient postage stamp production capacity to provide competition. The number of companies competing for contracts to produce postage stamps has increased, and the private sector stamp production capability and capacity has expanded in the last decade. As the private sector production capabilities expanded, a sufficient overlap in similar products produced by the Bureau and the private sector occurred that now makes equitable cost comparisons possible. GAO's comparison of costs on selected pairs of comparable stamps produced by the Bureau and

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private sector contractors showed that for seven of eight selected pairs of stamps, the cost for stamps produced by private sector contractors was lower than the cost for Bureau products.

Although the Postal Service's procedures for monitoring quality differ from the private sector to the Bureau, quality deficiencies have been found in stamps produced by both the Bureau and the private sector.

The relationship between the Bureau and the Postal Service has greatly improved since the late 1980s, primarily as a result of a formal interagency agreement that put the relationship between the Postal Service and the Bureau on a businesslike basis. The Postal Service now expects the Bureau to remain the principal provider of postage stamps.

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## Principal Findings

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### Private Sector Competition and Capacity

From 1978 through 1987, although there were two or more competing bidders for each stamp production contract, only one company, the American Bank Note Company, was awarded contracts as the low bidder. Since 1986, the Postal Service has increased sources of stamp production in the private sector through split procurements, multiple awards, changing from sealed bids to competitive negotiated procurements, and hosting annual stamp printers conferences. (See pp. 14-15.) However, these efforts to foster competition in the private sector were hampered by a series of mergers, acquisitions, and staff moves among companies, which led to questions aired in the philatelic press and at the June 1991 hearing about whether true competition existed among the private sector companies. However, a July 1991 Postal Inspection Service investigation of the postage stamp procurement process found no evidence to support suspicions of tainted relationships among companies or of improprieties associated with the solicitation and award of private sector stamp manufacturing contracts.

GAO found that all 21 private sector contracts awarded since January 1, 1987, by the Postal Service had had two or more offers in response to stamp procurement solicitations. The number of private sector companies submitting offers in response to solicitations is increasing. In the two most recent solicitations, six companies responded to one, and eight companies responded to the other. The Postal Service currently has 15 active

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contracts for postage stamps that have been awarded to 8 prime contractors. (See pp. 15-16.)

GAO surveyed the private sector contractors and found that, according to company officials, with their current staff, equipment, and hours of operation, they have the production capacity to annually produce about 73 billion water-activated postage stamps and about 20 billion pressure sensitive stamps. For fiscal year 1992, the Postal Service estimated that it will purchase a total of 57 billion stamps. Although the private sector production capacity has expanded significantly, it remains a developing industry. Limitations still exist in two areas—capacity for the more complex (intaglio) printing method and stamp finishing capacity. (See pp. 16-18.)

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## Comparison of Bureau and Private Sector Costs

For several years the differences in printing methods and formats used in the private sector and the Bureau prevented equitable cost comparisons. However, as the private sector production capabilities expanded, a sufficient overlap in similar products occurred that now makes equitable cost comparisons possible.

GAO matched stamp items produced by the Bureau with those produced by the private sector on four factors—(1) printing method, (2) finishing format, (3) stamp size, and (4) quantity produced—and found eight pairs of comparable stamps. The 16 selected stamp items represented 9 percent of the 187 stamp items produced in 1991. (See pp. 25-26.)

GAO first compared the prices the Postal Service paid to the Bureau and to the private sector for each stamp item and found that for 7 of the 8 pairs of stamps, the price paid per 1,000 stamps ranged from \$.20 to \$9.49 lower for private sector stamps than for Bureau stamps. GAO then adjusted the prices paid for stamps to reflect the total cost to the government for procuring postage stamps. The adjustments to the prices included such identified costs as personnel salaries and benefits, travel, rent, unfunded personnel benefits, and the estimated value of taxes paid by private sector stamp producers. GAO then compared the adjusted costs for procuring stamps and again found that for seven of the eight pairs of stamps the cost of procuring the stamps from the private sector was still from \$.13 to \$8.18 lower than procuring stamps from the Bureau. Adjusting the price to include all identified costs of procuring the stamps did not significantly change the overall results of the cost comparison. (See pp. 26-27.)

Although the private sector was a lower cost source for seven of the eight pairs of postage stamps, the Postal Service should keep the Bureau in a significant role as a stable provider of stamps. The Postal Service needs an experienced, stable supplier that is immune to union strikes, bankruptcies, and other problems that can plague private industry. As reported by GAO in 1991—U.S. Mint: Procurement of Clad Metal for Coins (GAO/GGD-91-78BR, May 17, 1991)—the government may become vulnerable to the narrowing of competition among private firms or to disruptions in private markets if it gives up a government production capability. The Postal Service can preclude this possibility by keeping the Bureau as a continuing—but not exclusive—source of supply. (See pp. 27-28.)

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### Monitoring Stamp Quality

Although the Bureau and the private sector are subject to the same product quality standards, the Postal Service does direct, on-site program and product monitoring at private sector manufacturing facilities, while at the Bureau it basically reviews the records of auditing and tracking procedures. However, Postal Service product deficiency documents noted quality deficiencies in Bureau products as well as private sector products, which indicates that neither is immune to quality control problems. According to Postal Service officials, there is no significant difference in the quality of stamps produced by the Bureau and the private sector. (See pp. 20-23.)

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### Relationship Between the Postal Service and the Bureau

In the late 1980s, the relationship between the Postal Service and the Bureau deteriorated until there was an almost total communications breakdown. The acrimonious relationship, which resulted from disagreements over stamp quality issues and related costs, eventually led to questions about the future stamp production role of the Bureau. In response to GAO's report, Postage Stamp Production: The Bureau of Engraving and Printing's Future Role (GAO/GGD-90-25, Dec. 12, 1989), the two agencies originally developed a formal interagency agreement in 1990 that put the Postal Service's and the Bureau's relationship on a businesslike basis. According to both Postal Service and Bureau officials, the problems identified at the June 1991 congressional hearing were addressed by the current agreement completed in March 1992. Officials in both agencies said that the agreement provides the basis for resolving problems and working together for long-term cultural changes. They also reported that their relationship is much improved over what it was a few years ago and attributed the improvements to better communication resulting from the agreement. The agreement appears to be working well and is an effective

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mechanism for resolving problems. As the agreement evolves through the annual negotiation process, it will further clarify expectations and requirements and better define the roles of the Postal Service and the Bureau in producing stamps. (See pp. 29-31.)

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## Recommendations

Because the Postal Service is continuing its initiative to seek lower stamp costs and develop additional sources of stamp production while ensuring a quality product, GAO is making no recommendations.

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## Agency Comments

In commenting on a draft of this report, the Postal Service agreed with the report's principal findings and said that by moving ahead with its initiative to procure stamp products from both the Bureau and private contractors, it will secure adequate, competitive, and reliable sources of production that will meet the nation's present and future stamp needs.

The Bureau said that the report provides a reasonable basis for responding to the questions from the Subcommittee. However, the Bureau raised two major concerns, saying first that the report does not adequately convey that the results of the cost comparison cannot be projected to other stamps. GAO believes the report clearly states that the comparison results apply only to the eight pairs of stamps and cannot be projected to other stamps.

The Bureau also said that the report does not recognize the value to the Postal Service of the secure, stable production capacity maintained by the Bureau that should have been included in the cost comparison. GAO saw no need to quantify the cost and value of establishing and maintaining the Bureau's production capacity because GAO agrees that it is necessary to maintain the Bureau as a stable, secure source of stamps.

Chapter 6 discusses the comments made by the two agencies; their comments are presented in appendixes IV and V. Technical comments submitted by the Bureau were incorporated into the report as appropriate.



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**Abbreviations**

ABN	American Bank Note Company
GSA	General Services Administration
OMB	Office of Management and Budget

# Introduction

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Postal Service figures show that in fiscal year 1991, it procured approximately 54 billion postage stamps. Approximately 40 billion stamps were procured from the Bureau of Engraving and Printing, and approximately 14 billion were procured from the private sector. These stamps cost the Postal Service approximately \$124 million.

Most stamps are used to post mail. However, some are sold to stamp collectors and never enter the mail stream. These include "philatelic" stamps that are selected from regular stamp issues on the basis of their near-perfect aesthetic characteristics for sale through the Postal Service's mail order facility in Kansas City, Missouri, and philatelic windows located in some post offices. According to the Director, Office of Stamp and Philatelic Marketing, most stamps bought by collectors are purchased through the more than 100,000 post offices, vending machines, and retail stores. Stamps sold to collectors are high-profit items for the Postal Service because collectors retain most of them, thereby sparing the Postal Service from providing mail delivery service. The Postal Service received \$162 million from stamps sold to and retained by collectors in fiscal year 1991.

The Department of the Treasury's Bureau of Engraving and Printing has produced most of the Postal Service's (and its predecessor, the Post Office Department's) stamp requirements for nearly 100 years. The Bureau's production facility is located in Washington, D.C. In fiscal year 1991, currency production for the Federal Reserve accounted for about 70 percent of the Bureau's total revenue, while stamp production accounted for about 28 percent.

The Postal Service is not legally required to obtain its stamps from a government supplier and in 1978 began contracting out for selected stamp issues. A major impetus for the Postal Service's initiative to procure stamps from the private sector was the deterioration of relations between the Postal Service and the Bureau that resulted primarily from disagreements over stamp quality issues and related costs. The agencies' inability to resolve the disagreements resulted in their relationship deteriorating from 1985 until the almost total communication breakdown that occurred in 1988. In June 1988, the Postmaster General wrote to the Secretary of the Treasury, resurrecting a 1982 privatization initiative by Treasury, and suggested that all postage stamp production should be contracted out to the private sector within 5 years. In the 1991 hearing, we testified that Postal Service and Bureau officials agreed that the acrimonious relationship that divided the two agencies in past years was

much improved.<sup>1</sup> The improvement was ascribed to the development, in response to our 1989 recommendations,<sup>2</sup> of a formal interagency agreement that was worked out over several months of intensive negotiations.

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## Stamp Manufacturing Process—Printing Methods and Formats

Stamp production is a complicated process that includes stamp designing, engraving, printing, perforating, packaging, storing, and distributing. Stamps are printed using the gravure, intaglio, offset, and intaglio/offset combination methods. Printed sheets are then perforated and processed into sheet, booklet, and coil formats.

In the intaglio method of printing, the image is hand cut or engraved into the surface of a master die and transferred to a steel print cylinder or plate. During the printing process, the cylinder or plate is coated with ink to fill the recesses, and the surface is wiped clean so that only the recesses remain inked. The cylinder or plate is then applied to paper under great pressure, and the ink is pulled from its engraved recesses, creating a raised image on the surface of the paper. The resulting highly detailed textured product is difficult to reproduce and, therefore, difficult to counterfeit.

The gravure method is like the intaglio method in that the print image is transferred to the paper via an engraved print cylinder. However, the image is chemically or electronically etched into the surface of the print cylinder or plate, rather than hand-engraved. Instead of lines, small uniform-sized dots, or pits, result from the etching process. The printing process itself is much like the intaglio process in that ink is placed in the engraved areas of the cylinder, and paper is forced down into them. Gravure-printed products also have raised ink surfaces, but under magnification the ink is seen as a series of uniform-sized dots rather than solid lines.

The offset method uses an intermediate or offset cylinder to transfer the image from the printing cylinder/plate to the paper surface. Offset printing results in a smooth, clear image. This method is often used in combination with the intaglio method.

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## Objectives, Scope, and Methodology

In a June 1991 hearing, the Subcommittee on Postal Operations and Services, House Committee on Post Office and Civil Service, examined the

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<sup>1</sup>Postage Stamp Production and Procurement (GAO/T-GGD-91-39, June 5, 1991).

<sup>2</sup>The Bureau's role in postage stamp production was the subject of our report, *Postage Stamp Production: The Bureau of Engraving and Printing's Future Role* (GAO/GGD-90-25, Dec. 12, 1989).

production and procurement of postage stamps. Testifying at the hearing were a stamp manufacturer, two philatelists, and representatives from the Bureau of Engraving and Printing, the U.S. Postal Service, and GAO.<sup>3</sup> Information provided by these witnesses raised questions (subsequently referred to us) about (1) the production capacity and competitive nature of private sector stamp manufacturers, (2) steps taken by the Postal Service to monitor the quality and security of stamps, (3) whether Bureau prices could be compared with private sector prices, and (4) whether further improvements are needed in the relationship between the Bureau and the Postal Service.

To examine the competitive nature of private sector stamp manufacturers, we reviewed all Postal Service contracts open as of November 1991 and contracts awarded from November 1991 through June 15, 1992; the Deloitte and Touche 1990 Study of Stamp Production via the Private Sector; and a July 1991 Postal Inspection Service report on Postal Service contracts for postage stamps. Estimates of production capacity were provided orally by seven stamp manufacturers.

To determine the procedures the Postal Service follows to monitor the quality and security of stamps, we interviewed officials in the Postal Service's Stamp Manufacturing Division and Postal Inspection Service and observed two Postal Service product verification inspections at a contractor's manufacturing facility. We reviewed various Postal Service quality assurance documents. In addition, we reviewed corrective action requests for June 1991 through April 1992, corrective action request letters for April 1991 through April 1992, Postal Service Test and Evaluation Division test results for February 1991 through April 1992, and stamp discrepancy reports for the first quarter of fiscal year 1992.

To determine whether Bureau prices could be compared with private sector prices, we examined the 187 stamp items manufactured in 1991. We matched stamp items produced by the Bureau to those produced by the private sector on four factors—(1) printing method, (2) finishing format, (3) stamp size, and (4) quantity produced—and identified eight pairs of comparable stamp items. We then adjusted the prices paid for stamps to account for the total costs to the government in procuring postage stamps. The results apply only to the eight pairs of stamp items and cannot be projected to the other stamp items. (Details on our cost comparison methodology are included in app. I.)

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<sup>3</sup>GAO/T-GGD-91-39, June 5, 1991.

To determine whether further improvements are needed in the relationship between the Bureau and the Postal Service, we reviewed the June 1990 and March 1992 versions of the Agreement Between the Bureau of Engraving and Printing and the United States Postal Service for Production of Postage Stamps. We discussed interagency working relationships with the Director and key officials at the Bureau of Engraving and Printing and the Director, Office of Stamps and Philatelic Marketing, and the General Manager, Stamp Manufacturing Division, of the Postal Service. Information provided by GAO's December 1989 report<sup>4</sup> and the June 1991 testimony<sup>5</sup> was considered in doing this work.

We worked primarily at the U.S. Postal Service and Bureau of Engraving and Printing headquarters in Washington, D.C. We observed the Bureau's stamp production operation in Washington, D.C., as well as the American Bank Note Company's stamp production operations in Los Angeles, California, and Guilford, Connecticut. We did not independently verify agency data used in this report.

We did our work from September 1991 to June 1992 in accordance with generally accepted government auditing standards. The Postal Service and the Bureau provided written comments on a draft of this report. The text of the Postal Service's and Bureau's comments are presented in appendixes IV and V.

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<sup>4</sup>GAO/GGD-90-25.

<sup>5</sup>GAO/T-GGD-91-39.

# Private Sector's Capacity for Producing Stamps Is Expanding

In 1978, the Postal Service announced its intention to seek bids from private industry for the production of selected issues of postage stamps. One purpose of this initiative was to determine if "additional sources of stamp production" could be developed. Since 1978, the Postal Service has used several approaches to get more private sector companies involved, including split procurements, multiple awards, moving from sealed bid to competitive negotiated procurements, and hosting annual stamp printers conferences.

The Postal Service's stamp program was the subject of the June 1991 oversight hearings by the Subcommittee on Postal Operations and Services, House Committee on Post Office and Civil Service. During the hearings, a substantial discussion ensued in which the Subcommittee raised doubts about the relationships among the private sector companies. Its questions focused on the number of private sector companies involved in producing stamps, whether the number was sufficient to ensure healthy competition, and the stamp production capability of the private sector.

## Efforts to Increase Sources of Stamp Production

In 1978, the Postal Service awarded its first private sector contract for the production of postage stamps. The initial solicitation was sent to about 71 companies. Four responses were received—two from domestic and two from foreign sources. The "old" American Bank Note Company<sup>6</sup> was the successful bidder. From 1978 through 1987, although there were two or more bidders competing on subsequent Postal Service solicitations, only one company was awarded contracts as the lowest responsive, responsible bidder, American Bank Note Company. The contracts were basically for the production of sheet stamps.

In 1986, the Postal Service actively moved to encourage other companies to compete for contracts by splitting a 5-year procurement into two segments—a 2-1/2-year contract to cover the period from January 1987 to June 1989 and a second 2-1/2-year contract to cover July 1989 to December 1991. The Postal Service believed that providing for an expanded start-up time on the second solicitation would give other companies enough time to acquire the equipment needed to produce postage stamps that in turn would increase the number of companies bidding for the second contract. However, the old American Bank Note Company was again the low bidder on both solicitations.

<sup>6</sup>In July 1990, United States Banknote Company merged with International Banknote Company, Inc. (American Bank Note Company's parent company), to form the United States Banknote Corporation. American Bank Note Company is now a subsidiary of the United States Banknote Corporation.

Before 1988, all stamp contract awards were made under the formal advertised or sealed bid process, which required that all contract awards be made to the firm able to meet the Postal Service's requirements with the lowest price. Thereafter, the Postal Service moved to competitive proposals. Under this method, the Postal Service evaluates proposals on the basis of companies' technical capabilities as well as price. Since 1989, the Postal Service has evaluated approximately 50 proposals from about 15 firms.

In 1989, the Postal Service commissioned a study by the firm of Deloitte & Touche to evaluate stamp production alternatives via the private sector. The message of that study was basically that the private sector was ready to play an increasing role in the production of postage stamps. The Postal Service actively moved forward in 1990, when it hosted the first stamp printers conference and announced that the Postal Service intended to increase its reliance on the private sector. Over 75 representatives from 40 firms attended the first stamp printers conference. In the following year the Postal Service hosted a second stamp printers conference that 150 representatives from 72 firms attended.

Beginning in 1990, the Postal Service also began making multiple awards to get more companies involved (i.e., splitting the requirements for a particular type of stamp and awarding contracts to two or more companies when their proposals were competitive). Thus far, four Postal Service solicitations for proposals have resulted in the awarding of multiple contracts for producing postage stamps.

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## **Relationships and Competition Among Private Sector Stamp Producers**

The Postal Service's early efforts to increase the number of companies competing for contracts was hampered by a series of mergers, acquisitions, and personnel movement among companies. These events brought about several questions aired in the philatelic press and the June 1991 congressional hearing regarding the relationships among and independence of the private sector companies. A chronology outlining the mergers, acquisitions, and personnel moves that gave rise to the questions is provided in appendix III. The chronology illustrates that although the Postal Service awarded contracts to five companies, events after the contract awards, in effect, reduced the competitive base to two companies.

A July 1991 U.S. Postal Inspection Service investigation of the integrity of the stamp procurement process found no evidence to support allegations

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Private Sector's Capacity for Producing  
Stamps Is Expanding**

of tainted relationships among companies or of improprieties associated with the solicitation and award of private sector stamp manufacturing contracts.

More recently, the Postal Service's efforts to increase sources of stamp production have increased the number of private sector companies involved in producing postage stamps. In the past year, five additional companies have been awarded contracts to produce stamps. As table 2.1 shows, the Postal Service currently has 15 active contracts for postage stamps that have been awarded to 8 prime contractors.

**Table 2.1: Private Sector Companies Involved in Producing Postage Stamps Under Active Contracts as of June 15, 1992**

<b>Prime contractors</b>	<b>Number of contracts</b>	<b>Printing suppliers</b>	<b>Finishing suppliers</b>
American Bank Note Company	4	Guilford Gravure Multi-Color Corp.	Guilford Gravure
Ashton Potter	1	NA	NA
KCS Industries <sup>a</sup>	1	Sennett Enterprises The Press	NA
Stamp Venturers	5	J.W. Fergusson & Sons Canadian Banknote Company	KCS Industries
Banknote Corporation of America, Inc.	1	NA	NA
Dittler Bros., Inc.	1	NA	Voxcom-Web Printing
Avery Dennison	1	NA	NA
3M	1	National Label Corp.	National Label Corp.

NA = not applicable

<sup>a</sup>Contract was awarded before KCS's participation in Stamp Venturers partnership.

Our review of the Postal Service file of contracts for the production of postage stamps found that the Postal Service received two or more offers or proposals in response to each solicitation. The number of companies submitting offers or proposals ranged from two to eight. Of the two most recent solicitations, six companies responded to one, and eight companies responded to the other. This response rate indicates that the Postal Service has succeeded in its goal of expanding its supplier base.

**Private Sector Stamp  
Production Capacity**

Since 1978, when the Postal Service began acquiring stamps from the private sector, the number of postage stamps produced by the private sector has steadily increased. From 1978 through 1988, the number of

postage stamps manufactured by the private sector was less than 3 percent of the Postal Service's stamp program requirements. During fiscal years 1988, 1989, and 1990, approximately 8 to 9 percent of the Postal Service's stamp requirements were supplied by private industry. In fiscal year 1991, the private sector firms produced roughly 14 billion stamps, about 26 percent of the total stamp program. For fiscal year 1992, the Postal Service estimated that it will purchase about 26 billion stamps from private sector contractors, which is about 47 percent of the total stamps it expects to procure.

For several years, only postage stamps in sheet format were produced by the private sector. Now, according to private sector and Postal Service officials, private sector firms can produce both water-activated and pressure sensitive stamps by all printing methods and sheet, booklet, and coil stamp formats.

We surveyed the private sector firms to determine what their stamp production capacity was with current staff, equipment, and hours of operation. As shown in table 2.2, the private sector estimated it has the capacity to annually produce about 73 billion water-activated stamps. In addition, the five companies with contracts for the production of pressure sensitive postage stamps estimated they have the production capacity to annually produce about 20 billion pressure sensitive postage stamps.

**Table 2.2: Private Sector Annual Capacity for Water-Activated Stamp Production**

<b>Stamps</b>	<b>Capacity (in billions)</b>
Sheets	
Gravure	16.0
Intaglio & intaglio/offset	4.5
Offset	23.3
Booklets	12.7
Coils	
Of 100	5.6
Of 500, 3,000, and 10,000	10.5
<b>Total capacity</b>	<b>72.6</b>

Although private sector capability and capacity has expanded, private sector officials pointed out that limitations still exist in two areas—intaglio printing capacity and stamp finishing capacity. Less than 1 percent of the private sector stamps produced in fiscal year 1991 were printed by the intaglio method compared to 62 percent of the Bureau stamps. According

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**Private Sector's Capacity for Producing**  
**Stamps Is Expanding**

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to the private sector officials, if a secure market exists for stamps, the private sector will expand its capacity to meet any demand for stamps by the Postal Service.

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# Postal Service's Quality Monitoring Differs Between Private Sector and Bureau

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Discussions during the 1991 hearings about the Postal Service's development of quality standards and complaints about the quality of stamps produced by both the Bureau and the private sector raised questions about how the Postal Service monitors quality and if its procedures differ from the private sector to the Bureau. We found that private sector contractors and the Bureau are subject to the same quality assurance program standards and product quality standards. However, the Postal Service's role in monitoring quality in the private sector and the Bureau differs.

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## Status of Standards Development

The Postal Service's philosophy and methodology for quality assurance programs have been finalized in documents known as standards 22A and 27 (USPS-STD-22A and USPS-STD-27). Standard 22A applies to private sector suppliers and standard 27 to the Bureau. The basic difference between standard 22A and standard 27 is in the requirements for establishing security and accountability systems. Standard 27 recognizes the Bureau's long history as a stamp producer and accepts its existing accountability and security systems.

Table 3.1 shows the status of documents to be included in the Postal Service's standard quality assurance system.

**Chapter 3  
Postal Service's Quality Monitoring Differs  
Between Private Sector and Bureau**

**Table 3.1: Status of Program Standards and Requirements Documents**

	<b>Document</b>	<b>Status</b>
System requirements	<u>USPS Standard Quality Assurance System for Postage Stamps and Related Products</u> USPS-STD-22A	Final
	<u>USPS Standard Quality Assurance System for Postage Stamps and Related Products for the Bureau of Engraving and Printing</u> USPS-STD-27	Final
	Suppliers Security and Accountability Requirements	Draft
Product standard specifications	USPS Specification for Stamp Paper USPS-P-1191	Final
	Specification for Stamp Inks	Draft
	USPS Specification for Stamp Paper Pressure Sensitive Adhesive	Draft
	USPS Specification for Postage Stamp Performance Requirements	Draft
	USPS Stamp Standardization Drawings DL 1003000	Final
Program and product quality monitoring procedures	Stamp Manufacturing Division Quality Assurance Manual	Draft
	<u>Procurement Quality Assurance Handbook</u> AS-706	Final

To impose standards or requirements on the private sector, all the Postal Service has to do is make the standards a part of the contract. Even when the standards are in draft form they can be imposed on the private sector contractors. However, under the terms of the interagency agreement, the Postal Service cannot impose the standards or requirements on the Bureau unless the Bureau agrees to accept them. According to a Postal Service official, there is no assurance that the Bureau will accept the standards when they are final.

## Quality Assurance Monitoring Program

The monitoring of private sector product quality begins during the prepress phase and continues throughout the production process through final product inspection and acceptance. The Postal Service's Stamp Manufacturing Division's quality assurance staff is responsible for monitoring private sector suppliers' quality assurance programs and product quality. The procedures for monitoring the quality of postage

stamps during production and final acceptance procedures are set forth in the draft quality assurance manual.

The monitoring of private sector product quality begins with first-sheet approval. Private sector contractors submit sample sheets to the Stamp Manufacturing Division for preproduction approval of color and registration. Once approved, this sheet sets the production standard for the rest of the print run. First-sheet approval must be obtained before production can begin. During production the quality assurance staff monitors quality to verify that all stamps produced are as good as or better than the approved first sheet.

Private sector contractors also are to submit samples of the materials they will use in the product plus samples of all new production to the Postal Service's Test and Evaluation Division, Engineering Development Center, for "first article" testing of how the product will perform in the mail stream. In addition, any product in production more than 30 days is to be retested monthly with the same procedures. The Test and Evaluation Division is to report the test results to the Stamp Manufacturing Division. Private sector contractors also are to do their own first article and monthly testing and send the results to the Stamp Manufacturing Division. It is planned that once the quality assurance staff is confident that a supplier is capable of performing the tests and is performing them properly, the Test and Evaluation Division will cease doing redundant testing. However, the quality assurance staff plans to keep the option to do follow-up verification on tests performed by contractors.

During production, the quality assurance staff is to make visits to contractors' manufacturing facilities to verify that quality assurance system processes are operational and to check product quality. The frequency of the visits varies according to the contractor's production level and shipping actions.

The quality assurance staff does a final product verification inspection of private sector products before accepting the product. Private sector contractors cannot ship or deliver final products until they have undergone a final inspection and acceptance.

Like the private sector contractors, the Bureau also is to comply with the first sheet approval and first article test procedures. However, while the quality assurance staff does direct, on-site program and product monitoring at private sector manufacturing facilities, it does not monitor

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product quality during production at the Bureau. At the Bureau, the quality assurance staff basically reviews the records of the auditing and tracking procedures done by the Bureau.

No final product verification inspection and acceptance of Bureau products is done. The quality assurance staff does a monthly vault verification to inventory the quantities of stamps in the Bureau's vault.

The Postal Service's corrective action documents for April 1991 through April 1992, test results for February 1991 through April 1992, and discrepancy reports for the first quarter of fiscal year 1992 reported 18 types of deficiencies in Bureau products and 15 types of deficiencies in private sector products. According to a Postal Service official, although some deficiencies are more important than others, in the aggregate there is no significant difference in the quality of stamps produced by the Bureau and the private sector. The reported deficiencies are provided in table 3.2.

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**Table 3.2: Postal Service's Reported Product Deficiencies**

<b>Product deficiencies</b>	<b>Bureau</b>	<b>Private sector</b>
<b>Stamps</b>		
Cancellation ink—long drying time		x
Wet and blot test—loss of image	x	x
Phosphor taggant application uneven and inconsistent	x	
Phosphor meter unit readings did not meet luminescence requirements	x	x
Blank perforated paper in booklet	x	
No denomination printed on individual stamps	x	
Failed adhesive tack time test	x	
Printed surface delaminated from the gummed layer		x
Registration, cut-offs, and drags	x	
Extreme paper curl; could cause loose panes in books	x	
Sheets curl/wrap after unpacking	x	
Cracking of paper on folding	x	
Perforations off center on select stock	x	
<b>Finishing/formatting/packaging</b>		
Booklet cover slitting/guillotining not clean; edges very rough	x	
Booklet cover perforations/fold weak, comes apart in handling	x	
Booklet not assembled according to blueprint for center line of fold locations of cover and sheetlet		x
Booklet edges are not square		x
Last or outside booklet slit from collated strip has uneven edge trim		x
Booklets; defective cuts/folds		x
Sheets loose and/or not adhered in booklets		x
Booklets with missing or incorrect quantity of sheetlets	x	x
Dirt, smudges, and debris on top sheetlet		x
Bottom stamps may adhere to booklet cover	x	x
Sheets stuck together		x
Adhesive tape ruins stamps on coils	x	
Quantities incorrect, miscount	x	x
Problem with packaging/labeling	x	x

**Security Monitoring**

The Postal Inspection Service monitors contractors' compliance with security requirements. In addition to conducting pre-award surveys and

evaluating the security plans for proposed manufacturing facilities, the Inspection Service also is to conduct periodic, unannounced security surveys to determine if the contractor is complying with their security plan. Formal reports of survey results are to be submitted to headquarters for review and approval and forwarded to the contracting officials. Reporting to the contractor is to be done through the contracting official. When called for, the contracting official can request a formal response from the contractor as to what action the contractor will take to correct identified deficiencies.

The responsibility for monitoring security is primarily carried out by field inspectors. A field inspector is assigned security monitoring duty in each region in which a contractor has a facility that manufactures postage stamps. In addition to security monitoring visits every 3 to 6 months, field inspectors are to visit in response to requests from contractors on an as-needed basis.

According to an Inspection Service official, field inspectors have identified some deficiencies in contractor security systems but no serious security problems at contractor facilities. When deficiencies are found, the Inspection Service, the contracting staff, and the Stamp Manufacturing Division staff work with the contractor until deficiencies are corrected.

According to an Inspection Service official, the Postal Service has not monitored security at the Bureau because of the Bureau's long, successful history with its security system.

# Stamp Costs Lowered Through Competitive Procurement

Expanded private sector production capabilities have produced a sufficient overlay of similar products and have made equitable cost comparisons with the Bureau possible. Cost comparisons of eight selected pairs of water-activated stamps indicated that the private sector is a lower cost source of stamps. Seven of the eight comparisons revealed that the costs for private sector stamps were significantly lower than the Bureau's. These cost differentials showed that the cost of private sector stamps ranged from 6.8 to 62.4 percent lower than the cost of Bureau stamps.

A detailed description of our cost comparison methodology is provided in appendix I. The individual cost comparisons are provided in appendix II.

## Equitable Cost Comparisons Are Possible

The second purpose of the Postal Service's initiative to procure postage stamps from private industry was to determine if "stamp costs could be lowered through competitive bidding." The opening statement of the Chairman of the Subcommittee on Postal Operations and Services, House Committee on Post Office and Civil Service, at the 1991 hearing raised the issue of the relative cost efficiency of the private sector as compared to the Bureau. The ensuing discussions surfaced a lack of agreement on whether an equitable basis could be established to compare the Bureau's and the private sector's relative costs.

For several years the private sector produced primarily gravure stamps in sheets. The Bureau produced primarily intaglio stamps in booklets and coils. This difference in printing methods and formats prevented equitable cost comparisons. However, as the private sector production capabilities expanded to include a broader range of printing methods and formats, a sufficient overlap in similar products occurred that would permit equitable cost comparisons.

In fiscal year 1991, the Postal Service purchased a total of 187 different stamp items, 139 from the Bureau and 48 from the private sector. We matched the 139 stamp items produced by the Bureau to the 48 produced by the private sector on 4 factors—(1) printing method, (2) finishing format, (3) stamp size, and (4) quantity produced—and identified 8 sets of stamps that were sufficiently similar to permit cost comparisons. This is 9 percent of the stamp items purchased in 1991. The General Manager of the Postal Service's Stamp Manufacturing Division concurred that the eight sets of stamps were of sufficient similarity and quality to permit valid cost comparisons.

Represented in the eight sets of stamps are all major stamp printing methods and two of the three basic formats. Also represented are small, large, and jumbo stamp sizes. The quantities produced range from less than 3.2 million for 1 matched set to over 500 million for another set.

## **Comparisons Showed That Private Sector Stamps Are Less Costly Than Bureau Stamps**

We first compared the direct prices paid by the Postal Service for the stamps. In 7 of the 8 sets of comparable stamps, the prices paid per 1,000 stamps ranged from \$.20 to \$9.49 (10.5 to 64.8 percent) lower for private sector stamps than for Bureau stamps. For the other set of stamps, the price paid for the Bureau-produced stamp was 18 cents, or 12.5 percent, less than the private sector stamp.

We then adjusted the prices to reflect the total cost to the government for procuring stamps from the private sector and the Bureau. The adjustments to the prices included other costs incurred by the Postal Service directly related to the acquisition of stamps, such as personnel salaries and benefits, travel, and rent. We also adjusted for the estimated costs (to the government, though not to the Postal Service) of the Bureau's unfunded personnel benefits and rent, and the estimated value of the taxes paid by private sector stamp producers. Finally, we adjusted the cost of Bureau stamps to reflect additional order-taking and distribution services provided by the Bureau but not provided by the private sector.

The resulting comparison of the adjusted costs again showed that for 7 of the 8 sets of comparable stamps, the cost per 1,000 stamps ranged from \$.13 to \$8.18 (or 6.8 to 62.4 percent) lower for the private sector stamps. For the other set of stamps, the cost for the Bureau-produced stamp was 25 cents, or 16.4 percent, less than the private sector stamp. The price and adjusted cost differences between the Bureau-produced stamps and those of the private sector are shown in table 4.1. Adjusting the prices paid for Bureau and private sector stamps to include all identified costs of procuring the stamps did not significantly change the overall results of the cost comparison.

**Table 4.1: Price and Adjusted Cost Differences Between Private Sector- and Bureau-Produced Postage Stamps**  
Comparison differences per 1,000 stamps

Comparable stamp names	Price paid by Postal Service			Adjusted cost to government		
	Private sector	Bureau	Difference	Private sector	Bureau	Difference
Express Mail 8.75, Express Mail 14	7.26	16.75	9.49	7.28	15.46	8.18
Red Cloud, Chavez	1.70	1.90	0.20	1.78	1.91	0.13
Savings Bond, Porter	2.25	3.17	0.92	2.33	3.14	0.81
Basketball, Matzelinger	2.25	3.15	0.90	2.33	3.12	0.79
Balloon, Wood Duck	2.49	2.80	0.31	2.56	2.85	0.29
Wood Duck, Select Wood Duck, Select	2.49	4.84	2.35	2.56	4.95	2.39
Official Mail 04, Official Mail 19	1.27	3.61	2.34	1.36	3.62	2.26
Flag Clouds, Cardinal	1.44	1.26	0.18	1.52	1.28	0.24

These results apply only to the eight pairs of stamps and cannot be projected to other stamp items. But, as these comparisons show, the Postal Service has been able to lower the overall cost of stamps by fostering the development of a private sector stamp production industry.

Bureau officials pointed out that although prices for some comparable stamps are lower from the private sector, all things are not equal between the Bureau and the private sector. They said that there are substantial costs associated with the maintenance of a government production capability that cannot be quantified and are not incurred by the private sector in its job-by-job bidding process. We agree that the establishment and maintenance of the Bureau's stamp production capability has a value to the Postal Service. Therefore, we saw no need to quantify the cost and value because we believe that it is necessary to maintain the Bureau as a stable, secure source of stamps.

## The Bureau Should Continue as Stable Provider of Stamps

The private sector has proven itself to be a lower cost source of postage stamps, and the overall cost of stamps has been lowered as a consequence of competitive bidding in the private sector. However, the private sector still produces limited quantities of intaglio stamps.

The Postal Service is still in the process of building a private sector stamp producing industry. While the private sector industry matures, the Postal

Service needs an experienced, stable supplier that is immune to strikes, bankruptcies, and a host of other problems that can plague private industry.

When the private sector stamp producing industry matures, the Postal Service should evaluate the overall capabilities of the private sector and the Bureau to determine what the Bureau's long-term role should be. However, the Bureau should continue to play a significant role as a stable source of stamps to prevent possible disruption of supply. According to a Postal official, only the Bureau can provide this stable source of supply. The Postal Service expects the Bureau to remain the principal provider of postage stamps.

Our earlier review of the U.S. Mint's procurement of clad metal for coins<sup>7</sup> demonstrated that the government may become vulnerable to the narrowing of competition among private firms or to disruptions in private markets by giving up a governmental production capability. The Postal Service needs to preclude this possibility by keeping the Bureau as a continuing source of supply.

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<sup>7</sup>U.S. Mint: Procurement of Clad Metal for Coins (GAO/GGD-91-78BR, May 17, 1991).

# Postal Service/Bureau Relationship in the Production of Postage Stamps

Before fiscal year 1991, the relationship between the Postal Service and the Bureau was largely informal and, in the late 1980s, it had deteriorated until there was an almost total communication breakdown. The acrimonious relationship eventually led to questions as to whether the Bureau would have a future role in stamp production. In response to a 1989 GAO recommendation,<sup>8</sup> the two agencies negotiated for several months to develop a 5-year agreement and on June 11, 1990, the completion of the interagency agreement was accomplished. The agreement put the relationship between the Postal Service and the Bureau on a businesslike basis and resolved many of the problems that existed under the previous informal arrangement. The negotiations for the current agreement, completed in March 1992, further clarified expectations and improved the relationship between the two agencies.

## The Agreement

The purpose of the agreement is to provide the Postal Service with a reliable source for stamp production and provide the Bureau with a commitment by which it can project long-term planning of capital investment, research and development, inventory of supplies, and personnel needs. The agreement spells out detailed understandings and procedures in such areas as quality standards and verification, auditing of costs, communication responsibilities, and production lead-times. According to officials at both agencies, the agreement provides a mechanism for resolving future problems or differences that may arise.

## Term of the Agreement

The agreement, which was signed in June 1990, was initially established for a period of 5 years but could be renewed annually for additional 1-year periods. After each year, the agreement could be extended by mutual consent of the parties for a 1-year increment added to the remaining years. If such extension was not requested, or either party decided not to agree to such an extension, the agreement would terminate at the end of the current 5-year period. This arrangement enabled the agencies to have a 5-year agreement constantly in effect if they so chose.

The current agreement, which was signed in March 1992, provides for incremental increases in the term of the agreement that can result in a 10-year agreement in 1996. At the end of each fiscal year, the agencies will review the agreement and negotiate either to extend or terminate the agreement at the end of the last fiscal year already covered by the agreement. If the agencies agree to extend the term of the agreement, it

<sup>8</sup>GAO/GGD-90-25, Dec. 12, 1989.

shall be extended each fiscal year by adding additional years to the basic 5-year agreement. If the agreement is extended according to schedule, the agreement negotiated in 1996 will be a 10-year agreement.

## The Agreement as a Mechanism for Resolving Problems

During the June 1991 hearings, Bureau and Postal Service officials identified six issues (three for each agency) for the negotiations that began in the fall of 1991. The three issues identified by Bureau officials were the (1) reliability and timing of forecasts of stamp requirements, (2) billing and payment procedures, and (3) provision of quality standards for stamps. According to Bureau officials, the 1992 agreement resolved the first two issues and adequately addressed the third issue.

According to Bureau officials, the first issue concerned the Postal Service's unreliable projection of postage stamp requirements, which presented the Bureau with serious difficulties in material and equipment procurements as well as manpower and equipment utilization. The 1992 agreement changed the timing of the stamp forecasting cycle and established a base level number of stamps (as opposed to a percentage) to be supplied by the Bureau. According to Bureau officials, the 30 billion to 35 billion stamp level specified in the agreement is the optimum level for the efficient utilization of Bureau resources. With existing equipment, officials said the Bureau can produce about 50 billion stamps, but it would need to increase the number of staff in increments as the volume goes up. The 30 billion to 35 billion level is set in the agreement for the next 5 years. During each year's negotiations, the level for the years being added to the agreement will be negotiated. Bureau officials said these changes will allow the Bureau to do long-term planning.

The second issue dealt with the old billing and payment procedures under which the Bureau was paid when stamps were shipped from the storage vault. According to Bureau officials, the Bureau produces stamps to an order from the Postal Service, not to orders from the field. However, stamps were shipped from the vault to fill orders from postmasters in the field, and often certain issues were not ordered. The Bureau ended up storing stamps or carrying stock for the Postal Service over a period of time without getting paid for the stamps. Under the new procedures, at the end of each accounting period, the Bureau bills and the Postal Service pays for what was delivered to the vault.

The agreement addresses the third issue regarding the quality standards for stamps by providing that the Postal Service shall provide to the Bureau

by the end of fiscal year 1992 written product standards for each product type. The Bureau considers specific quality standards to be critical to its total quality management program. Bureau officials said they fully expect this provision to resolve the situation because the quality standards are doable, and the Postal Service is proceeding with developing the standards.

The three issues identified by Postal Service officials were (1) the extent to which the Bureau will use materials developed by the Postal Service, (2) whether the Bureau will adopt the Postal Service's quality assurance standards, and (3) whether the Bureau will package stamps as required by the Postal Service's distribution system. According to a Postal Service official, the subjects were recognized as long-term cultural changes and the agreement provides the basis for resolving the three issues. All three issues were addressed in the 1992 agreement and, according to the Director, Office of Stamp and Philatelic Marketing, the Postal Service is "quite satisfied" with the progress.

Officials in both agencies commented that the relationship between the Bureau and the Postal Service is much improved and far less contentious than what it was a few years ago. The primary factor to which they attribute the improvement is better communication.

The formal interagency agreement that put the relationship between the Postal Service and the Bureau on a businesslike basis is working well and appears to be an effective mechanism for resolving problems. However, the agreement is still evolving, and the Postal Service and the Bureau are continuing to work together to refine the agreement and address long-term issues through the annual renegotiation process. As expectations and requirements are further clarified in the agreement, it should help improve communication and production performance.

# Conclusions

The Postal Service's initiative to acquire postage stamps from the private sector appears to be succeeding. Its efforts to increase competition in the private sector have resulted in an increased number of companies competing for contracts, an expanding private sector stamp production capability and capacity, and no apparent difference in the quality of stamps produced by the Bureau and the private sector. In addition, on the basis of our cost comparisons, we found that the private sector is a lower cost source of postage stamps.

The relationship between the Bureau and the Postal Service has greatly improved since the late 1980s, primarily as the result of a formal interagency agreement that put the relationship between the Postal Service and the Bureau on a businesslike basis.

Although the private sector is a lower cost source of postage stamps, the Postal Service needs the Bureau as an experienced, stable supplier that is immune to problems that can plague private industry. The Postal Service now expects the Bureau to remain the principal provider of stamps. However, because the Postal Service is not required to purchase all or any of its stamps from the Bureau, the Bureau's future as the nation's stamp producer cannot be assured. As recently as 1988, the Postmaster General proposed contracting out all postage stamp production to the private sector.

When the private sector stamp producing industry matures, the Postal Service should evaluate the overall capabilities of the private sector and the Bureau to determine what the Bureau's long-term role should be. However, the Bureau should continue to play a significant role as a stable source of stamps. This will avoid the possibility of the Postal Service becoming vulnerable to the narrowing of competition among private firms or to disruptions in private markets.

## Agency Comments and Our Evaluation

In commenting on a draft of this report, the Postal Service agreed with the information presented, and the Bureau said that the report provides a reasonable basis for responding to the questions put forth by the Subcommittee. Their comments appear in appendixes IV and V. The Bureau also raised some concerns, which follow, that it believed should have been more fully addressed in the report.

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**Postal Service Comments**

The Postal Service said that by moving ahead with its initiative to procure stamp products from both the Bureau and private contractors, it will secure adequate, competitive, and reliable sources of production that will meet the nation's present and future stamp needs.

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**Bureau Comments**

The Bureau raised two main concerns, saying that the report does not adequately convey that the results of the cost comparison cannot be projected to the stamp program as a whole and does not recognize the value to the Postal Service of the secure, stable production capacity maintained by the Bureau that should have been included in the cost comparison. We recognize the Bureau's concern regarding the projectability of our results. In our attempt to make a fair comparison we looked only at stamps that were directly comparable. We believe that our report makes it clear that the results of the comparison cannot be projected to other stamps.

Regarding the Bureau's second concern, we agree in the report that the establishment and maintenance of the Bureau's stamp production capability has a value to the Postal Service. Therefore, we saw no need to quantify the cost and value of this stamp production capability. We also say in the report that the Bureau's continuing to play a significant role as a stable source of stamps should prevent possible disruption of supply and that the Postal Service expects the Bureau to remain the principal provider of postage stamps.

# Cost Comparison Methodology

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## Selection of Comparable Stamps

To determine if the cost of procuring stamps produced by private sector companies could be compared equitably with those produced by the Bureau, we examined the 187 stamp items<sup>1</sup> produced in fiscal year 1991. We matched the 139 stamp items produced by the Bureau to the 48 produced by the private sector on 4 factors or characteristics—printing method, finishing format, stamp size, and quantity produced. Our matching process identified eight pairs of postage stamps of sufficient similarity in the four factors to permit cost comparisons. A Postal Service official concurred that the selected pairs were of sufficient similarity to permit valid cost comparisons. Specific information regarding the selected pairs of stamps and their characteristics is included in appendix II.

The 8 pairs of stamps compose a 9-percent sample of the 187 stamp items purchased in fiscal year 1991. Represented in the eight pairs of stamps are the four major printing methods (gravure, intaglio, intaglio/offset, and offset), two of the three different finishing methods (sheets and booklets), and three of the four stamp size categories (small, large, and jumbo). The quantities produced for the matched pairs of stamps ranged from less than 3.2 million stamps to over 500 million stamps.

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## Cost Comparison

To estimate the total cost to the government of procuring stamps from the private sector and from the Bureau, we began with the prices paid by the Postal Service for the stamps. We then adjusted the prices to reflect (1) other costs incurred by the Postal Service directly related to the acquisition of stamps, (2) the estimated costs (to the government, but not to the Postal Service) of the Bureau's unfunded personnel benefits and rent, and (3) the estimated value of the taxes paid by private sector stamp producers.

In comparing the total cost to the government of acquiring stamps from the private sector and the Bureau, we made the following assumptions:

- We assumed that both the Bureau and the private sector faced essentially the same operating conditions and constraints (i.e., that both parties recovered all costs associated with stamp production and did not use other manufacturing operations to subsidize stamp production). However, we made one exception to this assumption. Because we were estimating the total cost to the government for acquiring stamps, we adjusted the cost

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<sup>1</sup>Often the same stamp issue is finished in different formats, i.e., sheets, booklets, or colls. Each format is considered a separate stamp item. A stamp issued in both booklets of 10 stamps and booklets of 20 stamps is counted as 2 separate stamp items. Stamps of the same issue and same format purchased from private sector companies at different prices are also counted as separate stamp items.

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for private sector stamps by the estimated taxes on revenue paid to the federal government by private sector companies. We made this adjustment because the Bureau does not pay taxes on revenue.

- We assumed a constant level of product quality between stamps produced by the Bureau and the private sector.
- We assumed that the Bureau and the private sector had similar types of equipment and used essentially the same types of processes to manufacture stamps. Thus, the production method to produce each pair of stamps was considered equivalent. A Postal Service official reviewed the pairs of selected stamps and concurred in this assumption.
- We assumed that services provided by the Bureau and the private sector companies were equivalent. However, there is one exception to this assumption. The Bureau provides a requisition filling service that the private sector does not provide. Our adjustment for this is detailed in the section explaining the adjustments to the cost of Bureau stamps.

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**Prices for Bureau and  
Private Sector Stamps**

For our comparison, we used the price provided us by the Bureau for each of the selected stamp items. The price reported by the Bureau is the annual weighted average price per 1,000 stamps for each of the selected stamps for fiscal year 1991. The Postal Service provided the prices for the private sector stamps on a price-per-1,000-stamp basis as well; these prices represent the actual prices billed to the Postal Service.

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**Costs Incurred by the  
Postal Service in Obtaining  
Stamps**

In addition to the prices paid for the stamps, the Postal Service incurred other costs that were directly related to the acquisition of stamps. These administrative costs included salaries and benefits for the related personnel in the Postal Service's Office of Stamp and Philatelic Marketing's Stamp Manufacturing Division, the Stamp Distribution Branch, the Stamp Administration and Advisory Branch, and the Philatelic Sales Division as well as the Postal Inspection Service, the Office of Procurement, and the Engineering and Development Center. The costs also included other such direct costs as travel and an estimated cost for rent for the utilized space.

The allocation of the administrative costs between acquiring stamps from the private sector and the Bureau was determined by the Postal Service and is shown in table I.1.

**Appendix I**  
**Cost Comparison Methodology**

**Table I.1: Allocation of Postal Service Administrative Costs**

Cost category	Total cost	Amount allocated to	
		Private sector	Bureau
<b>Personnel costs</b>			
<b>Salaries</b>			
Stamp Manufacturing Division	\$659,721	\$392,002	\$267,719
Office of Procurement	149,000	149,000	
Stamp Administration & Advisory Branch	267,533	267,533	
Inspection Service	14,891	14,891	
Stamp Distribution Branch	344,051	177,263	166,788
Philatelic Sales Division	9,792	6,336	3,456
Engineering & Development Center	167,165	46,748	120,417
Negotiation of Interagency Agreement	1,495		1,495
<b>Subtotal salaries</b>	<b>1,613,648</b>	<b>1,053,773</b>	<b>559,875</b>
Benefits (27.44% of salaries)	442,785	289,155	153,630
<b>Total personnel costs</b>	<b>2,056,433</b>	<b>1,342,928</b>	<b>713,505</b>
<b>Other direct costs</b>			
Stamp Manufacturing Division	18,039	18,039	
Stamp Distribution Branch	3,000	3,000	
Stamp Administration & Advisory Branch	3,811	3,811	
<b>Total other direct costs</b>	<b>24,850</b>	<b>24,850</b>	
Rent	80,032	52,821	27,211
<b>Total Postal Service costs</b>	<b>\$2,161,315</b>	<b>\$1,420,599</b>	<b>\$ 740,716</b>

We then calculated the Postal Service's administrative cost per 1,000 stamps and adjusted the cost of each of the selected stamp issues by this unit cost. For the unit cost per private sector stamp, we divided the total administrative costs allocated to the private sector (\$1,420,599) by the total number of stamps delivered by the private sector (13,822,690,000) to determine the unit cost of \$0.00010 per stamp, or \$.10 per 1,000 stamps. For the unit cost per Bureau stamp, we divided the total administrative costs allocated to the Bureau (\$740,716) by the total number of stamps delivered by the Bureau (39,820,625,200) to determine the unit cost of \$0.00002 per stamp, or \$.02 per 1,000 stamps.

**Other Cost Adjustments**

Several other adjustments to the cost for Bureau and private sector stamps were necessary to ensure that all relevant cost factors were considered.

**Adjustments to Costs of Bureau Stamps**

**Employee Benefits.** According to the Office of Personnel Management, the cost to the government for employee benefits is estimated at 27.44 percent of employee salaries and wages. In its pricing of stamps, the Bureau included 22 percent for the cost of employee benefits but did not include the unfunded portion of employee retirement costs incurred by the government. Therefore, to cover this unfunded liability, an adjustment of 5.39 percent of salaries and wages was made to the cost of the Bureau-produced stamps. The unfunded benefit cost associated with each of the selected stamps and the method of computation is shown in table I.2.

**Table I.2: Adjustments to Bureau Costs for Unfunded Employee Benefits**

Stamp name	Personnel cost per 1,000 stamps <sup>a</sup>	Number of stamps provided to Postal Service	Personnel costs <sup>b</sup>	Cost of salaries <sup>c</sup>	Cost of unfunded benefits <sup>d</sup>	Unfunded benefit per 1,000 stamps <sup>e</sup>
Red Cloud	\$.46	136,600,000	\$ 62,836.00	\$ 51,483.82	\$ 2,774.98	\$0.02
Savings Bonds	.81	150,560,000	121,953.60	99,921.02	5,385.74	0.04
Basketball	.80	150,060,000	120,048.00	98,359.69	5,301.59	0.04
Flag Clouds	.36	270,150,000	97,254.00	79,683.74	4,294.95	0.02
Express Mail	3.64	2,484,000	9,041.76	7,408.24	399.30	0.16
Official Mail	.48	6,070,000	2,913.60	2,387.22	128.67	0.02
Wood Duck, Select	2.34	6,390,000	14,952.60	12,251.21	660.34	0.10
Balloon	.85	632,712,000	537,805.20	440,643.34	23,750.68	0.04

Note: The total benefit rate of 27.44 percent of personnel salaries is the rate proposed in the draft revision to OMB Circular A-76, which is developed by the Office of Personnel Management. It includes agency retirement costs, federal employee insurance, miscellaneous fringe benefit costs, and Medicare costs.

<sup>a</sup>Personnel cost per 1,000 stamps as provided by the Bureau.

<sup>b</sup>Personnel cost per 1,000 stamps x (number of stamps divided by 1,000) = Bureau personnel cost (this included 22 percent benefits included in Bureau rates).

<sup>c</sup>Personnel cost divided by 1.2205 = Bureau salary cost.

<sup>d</sup>Cost of salaries x .0539 = the dollar value of the portion of the benefits excluded in the Bureau labor rate (5.39 percent).

<sup>e</sup>(Cost of unfunded benefits divided by the number of stamps) x 1,000.

**Rent.** The Department of the Treasury has custody of the building that houses postage stamp production and does not charge the Bureau rent. As a consequence, the Bureau does not include costs for the building itself in its charges to the Postal Service. To account for the cost of the occupied building space, we obtained an estimate of the rental cost from the General Services Administration (GSA). The cost estimate of \$13.43 per square foot is based on 80 percent of the cost of space at the Department of Agriculture at 14th Street and Independence Avenue (across the street from the Bureau) without charges for operations and maintenance services. Eighty percent of the office space rate is the standard rate GSA uses for light industrial space. The Bureau estimates that it uses approximately 150,000 square feet of space for stamp manufacturing. Therefore, we computed the cost adjustment factor by dividing the approximate annual rental cost (\$2,014,500) by the total number of stamps delivered to the Postal Service (39,820,625,200) to determine a unit cost of \$.00005 per stamp, or \$.05 per 1,000 stamps.

**Vaulting and Shipping.** While private sector stamp manufacturers deliver their stamps to the Postal Service, which then redistributes the stamps to postmasters and other retail outlets, the Bureau receives and fills requisitions from postmasters and delivers stamps to them directly. As a consequence, adjustments to the Bureau's costs were necessary to reflect the additional service. However, this service is included in the Bureau's charges for shipping and vaulting, and the Bureau could not provide an estimate for the cost of filling requisitions. We adjusted the cost for Bureau stamps by deleting the total cost per 1,000 stamps for vaulting and shipping for each of the stamp issues. We obtained the cost per 1,000 stamps for vaulting and shipping of each stamp from the Bureau. Table I.3 shows the amount of the adjustment for vaulting and shipping for each stamp.

**Table I.3: Adjustments to the Cost of Bureau Stamps for Vaulting and Shipping**

<b>Stamp</b>	<b>Amount of adjustment (per 1,000 stamps)</b>
Savings Bond	\$.14
Basketball	.14
Wood Duck, Select	.06
Balloon	.06
Red Cloud	.08
Express Mail	1.52
Official Mail	.08
Flag Clouds	.08

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**Adjustments to Costs of Private  
Sector Stamps**

Since stamp manufacturing provides the private sector suppliers with income that is subject to federal income tax, an estimated amount of such taxes should be deducted from the cost of private sector stamps. We used a rate of 1.1 percent of business receipts for commercial and other printing and printing trade services in the Tax Rate Table, which is prepared by the Internal Revenue Service and included in the supplement to OMB Circular A-76, "Performance of Commercial Activities," to develop the estimated taxes paid by the private sector.

The results of our cost comparison are detailed in appendix II.

# Comparisons of Selected Pairs of Stamps Produced by the Bureau and the Private Sector

	<b>Bureau</b>	<b>Private sector</b>
<b>Stamp name</b>	<b>Flag Clouds</b>	<b>Cardinal</b>
Printing method	Gravure	Gravure
Finishing format	Sheets of 100	Sheets of 100
Stamp size	Small	Small
Quantity (in millions)	270.15	193.45
Cost comparison		
Price per thousand	\$1.26	\$1.44
Adjustments:		
Vaulting & shipping	(0.08)	
Unfunded personnel benefit	0.02	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.02)
Net adjustments	0.01	0.08
<b>Adjusted cost of stamps</b>	<b>\$1.27</b>	<b>\$1.52</b>
<b>Stamp name</b>	<b>Savings Bond</b>	<b>Porter</b>
Printing method	Gravure	Gravure
Finishing format	Sheets of 50	Sheets of 50
Stamp size	Large	Large
Quantity (in millions)	150.56	149.85
Cost comparison		
Price per thousand	\$3.17	\$2.25
Adjustments:		
Vaulting & shipping	(0.14)	
Unfunded personnel benefit	0.04	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.02)
Net adjustments	(0.03)	0.08
<b>Adjusted cost of stamps</b>	<b>\$3.14</b>	<b>\$2.33</b>
<b>Stamp name</b>	<b>Basketball</b>	<b>Matzellinger</b>
Printing method	Gravure	Gravure
Finishing format	Sheets of 50	Sheets of 50
Stamp size	Large	Large
Quantity (in millions)	150.06	148.97
Cost comparison		
Price per thousand	\$3.15	\$2.25
Adjustments:		

(continued)

**Appendix II  
Comparisons of Selected Pairs of Stamps  
Produced by the Bureau and the Private  
Sector**

	<b>Bureau</b>	<b>Private sector</b>
Vaulting & shipping	(0.14)	
Unfunded personnel benefit	0.04	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.02)
Net adjustments	(0.03)	0.08
<b>Adjusted cost of stamps</b>	<b>\$3.12</b>	<b>\$2.33</b>
<b>Stamp name</b>	<b>Balloon</b>	<b>Wood Duck</b>
Printing method	Gravure	Gravure
Finishing format	Books of 20	Books of 20
Stamp size	Small	Small
Quantity (in millions)	632.712	501.168
Cost comparison		
Price per thousand	\$2.80	\$2.49
Adjustments:		
Vaulting & shipping	(0.06)	
Unfunded personnel benefit	0.04	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.03)
Net adjustments	0.05	0.07
<b>Adjusted cost of stamps</b>	<b>\$2.85</b>	<b>\$2.56</b>
<b>Stamp name</b>	<b>Wood Duck, Select</b>	<b>Wood Duck, Select</b>
Printing method	Gravure	Gravure
Finishing format	Panes of 10	Panes of 10
Stamp size	Small	Small
Quantity (in millions)	6.39	7.38
Cost comparison		
Price per thousand	\$4.84	\$2.49
Adjustments:		
Vaulting & shipping	(0.06)	
Unfunded personnel benefit	0.10	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.03)
Net adjustments	0.11	0.07
<b>Adjusted cost of stamps</b>	<b>\$4.95</b>	<b>\$2.56</b>
<b>Stamp name</b>	<b>Red Cloud</b>	<b>Chavez</b>
Printing method	Intaglio	Intaglio

(continued)

**Appendix II  
Comparisons of Selected Pairs of Stamps  
Produced by the Bureau and the Private  
Sector**

	<b>Bureau</b>	<b>Private sector</b>
Finishing format	Sheets of 100	Sheets of 100
Stamp size	Small	Small
Quantity (in millions)	136.60	120.81
<b>Cost comparison</b>		
Price per thousand	\$1.90	\$1.70
Adjustments:		
Vaulting & shipping	(0.08)	
Unfunded personnel benefit	0.02	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.02)
Net adjustments	0.01	0.08
<b>Adjusted cost of stamps</b>	<b>\$1.91</b>	<b>\$1.78</b>
<b>Stamp name</b>	<b>Express Mail 8.75</b>	<b>Express Mail 14</b>
Printing method	Intaglio/offset	Intaglio/offset
Finishing format	Sheets of 20	Sheets of 20
Stamp size	Jumbo	Jumbo
Quantity (in millions)	2.48	3.14
<b>Cost comparison</b>		
Price per thousand	\$16.75	\$7.26
Adjustments:		
Vaulting & shipping	(1.52)	
Unfunded personnel benefit	0.16	
Rent	0.05	
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.08)
Net adjustments	(1.29)	0.02
<b>Adjusted cost of stamps</b>	<b>\$15.46</b>	<b>\$7.28</b>
<b>Stamp name</b>	<b>Official Mail 04</b>	<b>Official Mail 19</b>
Printing method	Offset	Offset
Finishing format	Sheets of 100	Sheets of 100
Stamp size	Small	Small
Quantity (in millions)	6.07	30.00
<b>Cost comparison</b>		
Price per thousand	\$3.61	\$1.27
Adjustments:		
Vaulting & shipping	(0.08)	
Unfunded personnel benefit	0.02	
Rent	0.05	

(continued)

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**Appendix II**  
**Comparisons of Selected Pairs of Stamps**  
**Produced by the Bureau and the Private**  
**Sector**

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	<b>Bureau</b>	<b>Private sector</b>
Postal Service costs	0.02	0.10
Taxes (1.1%)	NA	(0.01)
Net adjustments	0.01	0.09
<b>Adjusted cost of stamps</b>	<b>\$3.62</b>	<b>\$1.36</b>

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# Chronology Outlining the Mergers, Acquisitions, and Personnel Moves in Private Sector Companies

Date	Activity
1978	American Bank Note Company (ABN) formed joint venture with J. W. Fergusson & Sons.
1983	J. W. Fergusson & Sons declined to participate in joint venture with ABN.
1983-84 to 1987	ABN leased Fergusson's facilities.
1987	Sennett Enterprises formed by a Vice President of ABN, Richard C. Sennett. After terminating employment with ABN, Sennett Enterprises became a subcontractor to ABN and leased Fergusson's facilities.
Jan. 4, 1989	Jeffries Banknote Company acquired by United States Banknote Company
July 1990	<p>United States Banknote Company (Jeffries Bank Note's parent company) merged with International Banknote Company, Inc. (ABN's parent company) and formed the United States Banknote Corporation.</p> <p>United States Banknote Corporation is the parent company for its subsidiary, ABN. ABN has two manufacturing facilities—Chicago and Los Angeles—that produce postage stamps. The Los Angeles facility was formerly known as Jeffries Bank Note Co.</p>
Sept. 1, 1990	<p>J. W. Fergusson &amp; Sons, Banta Corporation, and Sennett Enterprises formed a partnership—Stamp Venturers—to engage in manufacturing postage stamps. In this partnership</p> <ul style="list-style-type: none"> <li>— Sennett Enterprises is the managing partner and oversees the entire process (partnership name is Unique Binders, Inc.)</li> <li>— J. W. Fergusson supplies the press for the gravure printing process (partnership name is Fergusson Stamp Venture Group, Inc.)</li> <li>— Banta Corp. dedicated the KCS facility, personnel, and equipment for the finishing process. KCS is a subsidiary of Banta Corp. (partnership name is Banta Security Printing, Inc.). The Chairman of the Board of Banta and the Vice President for Manufacturing at KCS are former ABN officials.</li> </ul>

# Comments From the U.S. Postal Service



THE POSTMASTER GENERAL  
Washington, D.C. 20260 0010

October 15, 1992

Mr. Richard L. Fogel  
Assistant Comptroller General  
United States General Accounting Office  
Washington, D.C. 20548-0001

Dear Mr. Fogel:

Thank you for providing us an opportunity to comment on the draft report entitled, Postage Stamp Production: Private Sector Is a Lower Cost Optional Source. We agree with the report's principal findings that there is sufficient stamp production capacity and competition among private sector contractors to justify the Postal Service continuing to use them as an optional, lower cost source of procurement.

We believe that the report validates our position that a competitive environment for stamp production is in the best interests not only of the Postal Service but also of the public. We can continue to seek the most cost-effective stamp suppliers while offering the public the high-quality mix of stamp products they expect.

We also agree that our relations with the Bureau of Engraving and Printing have improved over the past several years. As your report states, the Bureau is an experienced, stable supplier and we will continue to rely upon the Bureau to balance the relative youth and inexperience of the private sector.

By moving ahead with our initiative to procure stamp products from both the Bureau and private contractors, the Postal Service can secure adequate, competitive and reliable sources of production that will meet the nation's present and future stamp needs.

Best regards,

Marvin Runyon

# Comments From the Bureau of Engraving and Printing



DIRECTOR

DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING  
WASHINGTON, D.C. 20228

September 30, 1992

Richard L. Fogel  
Assistant Comptroller General  
U.S. General Accounting Office  
Washington, D.C.

Dear Mr. Fogel:

Thank you for the opportunity to review the draft GAO report entitled Postage Stamp Production: Private Sector is a Lower Cost Optional Source. In general, we believe that this report provides a reasonable basis for responding to the questions put forth by the Chairman of the Subcommittee on Postal Operations and Services, House Committee on Post Office and Civil Service. However, we believe that the report would be improved if the following factors were incorporated.

Although the report indicates that the cost comparison of the eight pairs of stamps applies "only to the 8 pairs of stamps and cannot be projected to other stamp issues", the title of the report "Postage Stamp Production: Private Sector is a Lower Cost Optional Source", conveys the impression that private sector cost is lower overall. We believe that changing the title to "Postage Stamp Production: Private Sector is a Lower Cost Option For Selected Issues" would more accurately represent the findings of the report. The first sentence of the last paragraph on page 7 of the draft report should also be revised to state that the private sector was a lower cost source for 7 of the 8 pairs of stamps.

As a matter of public policy, the Bureau of Engraving and Printing believes that there is a sufficient demand for United States postage stamps for both the private sector and the Bureau to play significant roles. However, the Bureau does not compete against the private sector, although it is capable of meeting the entire demand for postage stamps. Instead, the Bureau offers an established, state-of-the-art production capability, with all supporting systems necessary to assure that the USPS has a reliable and safe source of postage stamps. Consequently, the public policy question is to what extent this capability should be utilized and developed.

Now on p. 5.

**Appendix V  
Comments From the Bureau of Engraving  
and Printing**

As discussed with representatives from GAO, we take exception to certain assumptions and adjustments made in the cost comparison presented in the report. In our opinion, the cost comparison provides a snap shot of price comparability that existed during the fiscal year 1991 for a very small portion of the stamp program. No comparability analysis was done for the remaining 95% of the stamp volume that was produced by the private sector (24%) and the Bureau (71%). Therefore, it is not appropriate to extrapolate this comparison to the program as a whole. Furthermore, the most cost effective stamp program that could be produced by BEP would be much different than the program assigned to us today. Insufficient information exists to determine the long-term price comparability between the private sector and the Bureau, since GAO did not have information to determine the comparability of the costing principles used by the private sector and the Bureau. Thus, statements in the report that indicate that the private sector "is a lower cost source", (pages 7, 42, and 50), or that "stamp costs were lowered through competitive procurement" (pages 37, 41, and 42) seem erroneous.

Notwithstanding the price comparison that is presented in the report, there are inherent differences in the mission between the Bureau and the private sector. The private sector mission is to earn profit, and the firms involved in postage stamp production usually do so by a network of temporary production arrangements which expire when the stamp is produced to contract volumes. As the government's producer of postage stamps, however, the Bureau's mission is to provide a safe, flexible, and resilient production capacity so that it can quickly meet any Postal Service requirements for high-quality stamps in the most cost effective manner possible. As a consequence of this mission, the Bureau has established, at the request of the Postal Service, a multi-product capacity which exceeds the Postal Service's current requirements for stamps in all formats and from all printing methods. At the present time, about 50% of this production capacity is required to meet BEP's production schedule for postage stamps. The remaining reserve capacity provides the Postal Service with the insurance to contract stamps to the private sector at virtually no risk that the demand could not be filled by the Bureau should the private firm fail to deliver - and this has occurred. However, acquiring, maintaining and continually improving such reserve capacity carries fixed costs which affect the Bureau's prices for individual postage stamps, since there are not other users to absorb the costs for this equipment, and the Bureau is not able to bid on other work as its private sector counterparts are. There is, therefore, an inherent cost and value to the Postal Service of maintaining a secure reserve production capacity at BEP which should be recognized in the comparisons as an asset.

Now on pp. 5, 27, and 32.  
Now on pp. 25 and 27.

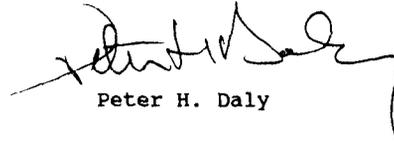
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**Appendix V  
Comments From the Bureau of Engraving  
and Printing**

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If you desire any additional information in this regard,  
please contact Paul Blackmer, Chief Financial Officer, on  
874-2020.

Sincerely,



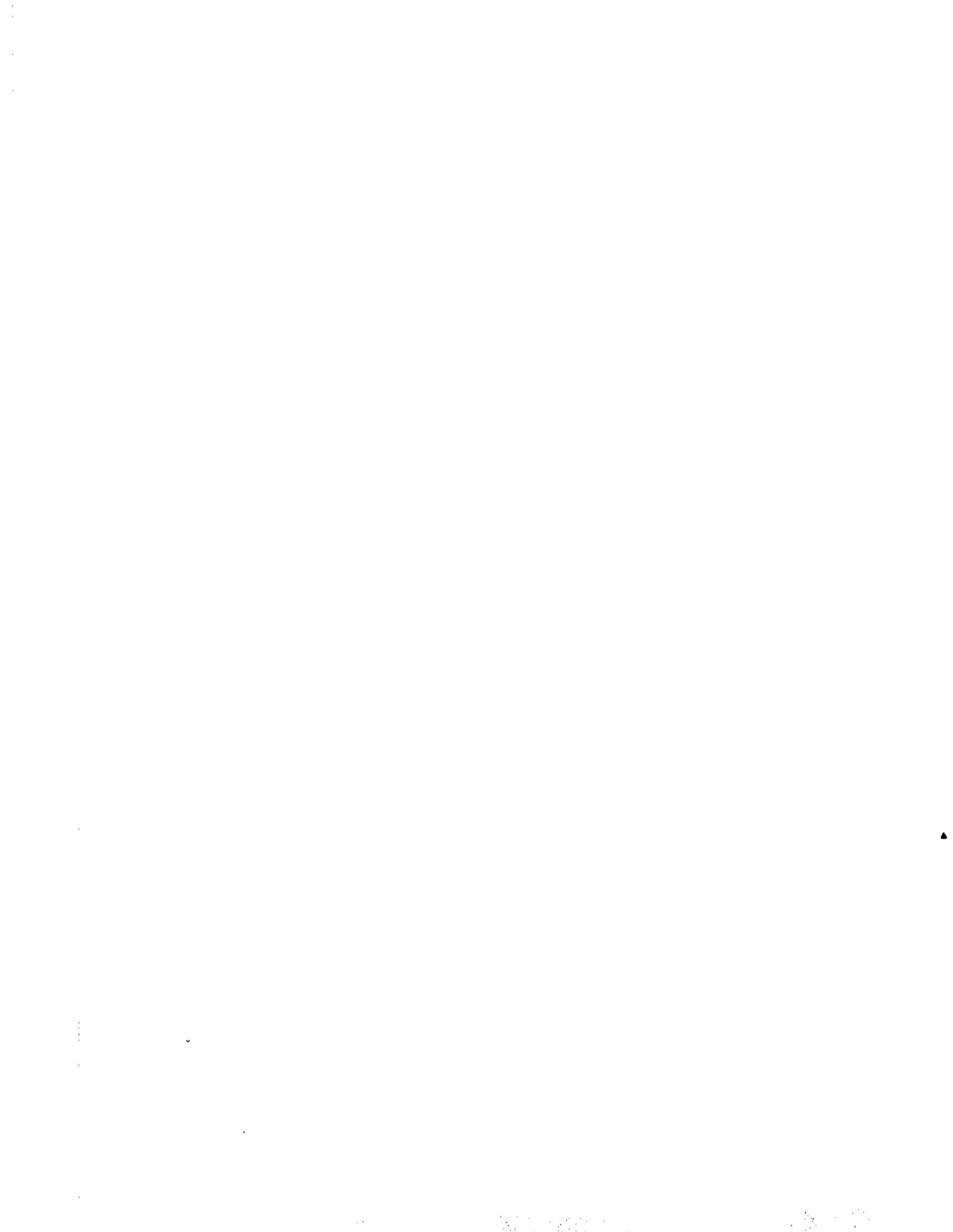
Peter H. Daly

# Major Contributors to This Report

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**General Government  
Division, Washington,  
D.C.**

**Willis Elmore, Assistant Director, Government Business Operations Issues  
Frances Clark, Assistant Director, Government Business Operations Issues  
Loretta Walch, Evaluator-in-Charge  
Carolyn Peake, Evaluator**



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